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Supreme Court of the United States

OCTOBER TERM, 1991

FRANKLIN FEDERAL SAVINGS BANK, *et al.*,
Petitioners,

v.

DIRECTOR, OFFICE OF THRIFT SUPERVISION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

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REPLY MEMORANDUM TO BRIEF FOR THE RESPONDENTS IN OPPOSITION

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ARGUMENT

1. The government does not disagree with petitioners' conclusion that the issue presented before this Court is one of national importance that is being litigated repeatedly throughout the federal court system. Indeed, four courts of appeals (and dozens of district courts) currently are addressing controversies in which the respective courts must decide whether the Financial Institu-

tions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"), Pub. L. No. 101-73, 103 Stat. 183, abrogates or preserves contracts entered into by the Federal Home Loan Bank Board ("FHLBB") or the Federal Savings and Loan Insurance Corporation ("FSLIC"), the predecessor agencies to the Office of Thrift Supervision ("OTS") and the Federal Deposit Insurance Corporation ("FDIC"), respectively.[1] The importance to which the government attaches to the issue has been underscored by its decision to have the Solicitor General make the argument next month in the United States Court of Appeals for the Third Circuit in *Carteret Savings Bank v. Office of Thrift Supervision*, No. 91-5290 (3d Cir. filed March 25, 1991).[2]

2. Respondents concede that Section 401(g) preserves contracts entered into by either the FHLBB or the FSLIC notwithstanding the abolition of these agencies in the FIRREA. Resp. Br. at 8. The government argues, however, that petitioners' contract is not abrogated by

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[1] *See Far West Federal Bank, S.B. v. Director, Office of Thrift Supervision*, No. 90-35752 (9th Cir. filed Sept. 19, 1990); *Sterling Savings Association v. Ryan, Director, Office of Thrift Supervision*, No. 91-35101 (9th Cir. filed Dec. 27, 1990); *Carteret Savings Bank v. Office of Thrift Supervision*, No. 91-5290 (3d Cir. filed March 25, 1991); *Security Savings & Loan Association, et al. v. Director, Office of Thrift Supervision*, No. 91-1570 (5th Cir. filed May 24, 1991); *Northeast Savings, F.A. v. Director, Office of Thrift Supervision*, No. 91-5226 (D.C. Cir. filed July 17, 1997); and *Transohio Savings Bank, et al. v. Director, Office of Thrift Supervision, et al.*, Civil Action Number not yet assigned (D.C. Cir. filed Aug. 8, 1991).

[2] While the government suggests that this Court should wait to review the issue until there is a conflict in the court of appeals, *see* Brief for the Respondents in Opposition ("Resp. Br.") at 8, delay in the resolution of the issue likely will lead to the seizure and liquidation of a number of healthy and viable savings and loan associations (including petitioner Franklin Federal Savings Bank) on a basis that this Court eventually may hold unlawful. In the interim, the government and thrifts alike will continue to expend enormous resources to litigate the instant issue.

virtue of the abolition of these agencies, but rather, by virtue of Section 301 of the FIRREA. The government's strained interpretation of the FIRREA implies that Congress, having made the determination in Section 401(g) to honor the government's commitments notwithstanding the abolition of the FHLBB and FSLIC, decided contemporaneously to abrogate the identical contracts in Section 301. The court of appeals erred for adopting the agencies' reading of the FIRREA, especially in light of the total absence of any language in the statute that explicitly terminates petitioners' contract rights.

3. The government suggests that the language of Section 401(g) should not be given its full effect because it is a "ministerial savings provision." *See* Resp. Br. at 9. But the government's logic would frustrate "the elementary canon of construction that a statute should be interpreted so as not to render one part inoperative." *Mountain States Tel. & Tel. Co. v. Pueblo of Santa Ana*, 472 U.S. 237, 249 (1985), quoting *Colautti v. Franklin*, 439 U.S. 379, 392 (1979). In any event, savings provisions that "are calculated to prevent hardship by saving accrued rights . . . from the operation of a new rule" are to be broadly construed. 2A N. Singer, *Sutherland Statutory Construction*, ¶ 47.12 at 149 (Sands 4th ed. 1984). *See also De La Rama S.S. Co. v. United States*, 344 U.S. 386, 389-90 (1953).[3]

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[3] The government gratuitously opines: "Congress recognized that one cause of the great losses suffered by taxpayers was past reliance by thrifts on intangible assets of illusory value." Resp. Br. at 8. But it was the offer of supervisory goodwill that induced the seven investors that comprise petitioner Franklin Financial Group, Inc. to acquire the institution and infuse $5 million of their own capital into the bank. Since the acquisition, the institution has earned approximately $1 million a year. In this context, it is apparent that the offer and use of supervisory goodwill, far from causing any losses, has "inured to the benefit of the F.D.I.C. [Federal Deposit Insurance Corporation] and the American public to a total sum of over seven million dollars." Order Granting Permanent Injunction ("Order") at ¶ 7, No. CIV-2-90-166 (E.D.Tenn. 1990) (Pet. App.

4. Respondents argue that Section 401(h) rather than Section 401(g) accords OTS the authority to "modif[y], terminate[], set aside, or supersede[]" petitioners' contract rights. Resp. Br. at 9. But the section to which the government refers only pertains to "orders, resolutions, determinations, and regulations"—all of which are *unilaterally* issued and may be *unilaterally* withdrawn. By contrast, Section 401(g) specifically pertains to "dut[ies]," and "obligation[s]"—which, by their nature, are binding on the parties and which may not be unilaterally withdrawn. Because petitioners' appeal assumes the existence of a contractual agreement, *see infra* at 5, Section 401(h) is irrelevant to this Court's analysis.

5. While Section 301 of the FIRREA appears to limit a savings association's use of supervisory goodwill for regulatory capital purposes, the section is silent as to whether it is intended to terminate contractual rights that are inconsistent with its provisions. It is a fundamental principle of statutory construction, however, that Congress, when it intends to upset settled expectations, must express its intention in *unmistakable* language. *See* cases cited in Petition at 15-17.[4] The government accepts this principle but argues that (1) petitioners never entered into a contractual relationship with respondents' predecessors-in-interest, and (2) if petitioners did enter into a valid and binding contract, "such contracts are subject to subsequent legislation and are to be construed so as to avoid foreclosing the exercise of sovereign immunity." Resp. Br. at 10.

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at 30a). Further, it was the respondents' predecessors, not petitioners, that created the concept and offered the use of goodwill as an asset to private investors to lure private capital into an industry in desperate need of such capital.

[4] *See also Bell Telephone Co. of Pa. v. Federal Communications Commission*, 503 F.2d 1250, 1280 (3d Cir. 1984), *cert. denied*, 422 U.S. 1026 (1975) ("The Communications Act contains no express statement of an intention to authorize unilateral modification or abrogation of privately negotiated contracts").

The government's characterization of petitioners' Forbearance Letter as a mere "regulatory decision" is both incorrect and irrelevant. The government ignores the district court's conclusion that the Forbearance Letter "was an integral part of the entire agreement and was for the benetfi of all parties in order to recapitalize the failing institution . . . ." Order at ¶ 4 (Pet. App. at 29). Indeed, the seven investors that comprise the holding company "would not have invested five million dollars into this institution absent the forbearance agreement, inasmuch as Franklin Federal would have been insolvent and subject to closure at its inception . . . ." *Id.* at ¶ 5 (Pet. App. at 29a).[5]

Moreover, the status of petitioners' contract is not even an issue in this appeal because the court of appeals never addressed the question. It instead assumed, for purposes of its analysis, that the Forbearance Letter was part of a contract. The issue before this Court, then, is *not* whether the Forbearance Letter was part of a contract, but rather, whether the FIRREA abrogates petitioners' contract, assuming one exists. If this Court answers in the negative, the court of appeals will have its opportunity to address the district court's factual findings.[6]

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[5] *See also Charter Federal Savings Bank v. Director, Office of Thrift Supervision et al.*, No. 91-0012-A, slip op. (W.D. Va. Aug. 6, 1991) ("When a party wants to engage in conduct that is subject to an agency's regulatory authority, and the agency gives permission to engage in the conduct for a specified period, the party is justified in understanding that the agency is committed to allowing the conduct for the specified period. If the agency has received consideration for its permission, a contract is formed.").

[6] Respondents further confuse the matter by noting that the Voting and Disposition Rights/Dividend Agreement indicates that regulatory changes "may increase or decrease [Franklin Federal's] obligation under this Agreement." *See* Resp. Br. at 2, 10-11. The district court, however, had to reconcile this language with language contained in the Forbearance letter, which expressly waives the FSLIC's and the FHLBB's right to take any enforcement action

The government's backup argument—that contracts must be construed to avoid impinging on the exercise of sovereign immunity—has no application here. Even under the contract, OTS and FDIC may, and do, extensively regulate Franklin Federal. In any event, petitioners assume for purposes here that Congress, if it so chooses, *could* abrogate petitioners' contract. It is petitioners' position, however, that Congress chose not to exercise that authority.

The court of appeals, far from requiring explicit statutory language abrogating petitioners' contract rights, merely "infer[red]" that Congress intended to abrogate the contract and "effect a taking." *See* Pet. App. at 18a. As most of the district courts have recognized, the court of appeals' inference is unwarranted.

> That Congress would accomplish such a result by nothing more than mere innuendo, its intent disguised by a questionable inference, makes [abrogation] all the more doubtful . . . . Statutory authorization to effect a taking, which of course would be the case here, must be specific, either in terms of an express remedy for the act or explicit permission to perform the act . . . .[I]n this case there is neither.

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based on Franklin Federal's treatment of supervisory goodwill. The letter provides that

> [o]*ther than* actions to enforce the regulatory requirements *waived* in accordance with paragraph 1 [authorizing amortization of goodwill] and the statutory provisions authorizing imposition of the *waived* requirement, . . .

the FHLBB and FSLIC retain all of their statutory rights and powers. Forbearance Letter at 1. Thus, while both parties understood that Franklin Federal generally would be subject to changes in the regulations, the parties likewise understood that Franklin Federal's right to treat supervisory goodwill as an asset stood apart, that this was instead such a material term of the contract that respondents were without the right to revoke this term. Moreover, as noted above, the construction of the contract is not currently before this Court—only whether the contract, as interpreted by petitioners and the district court—has been abrogated by the FIRREA.

Sterling Savings Association v. Ryan, Director, Office of Thrift Supervision, 751 F. Supp. 871, 880 (E.D. Wash. 1990), *appeal docketed*, No. 91-35101 (9th Cir. filed Dec. 27, 1990). To be sure, this Court has repeatedly stated that statutes are to be construed "to avoid raising doubts of its constitutionality." *St. Martin Evangelical Lutheran Church v. South Dakota*, 451 U.S. 772, 780 (1981). *Accord, United States v. Security Indus. Bank*, 459 U.S. 70, 82 (1982).

In short, if Congress wanted to abrogate petitioners' contract rights and effect a taking, it had an affirmative obligation to state so expressly. Its failure to do so leaves the courts no choice but to assume that petitioners' contract remains valid, binding and enforceable on the parties.

Respectfully submitted,

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